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Montana House
House Tax Committee

Testimony of

Mark Baker

Regarding House Bill 626

EXHIBIT 6
DATE 3/24/11
HB 626

Mr. Chairman and members of the Committee, my name is Mark Baker and it is an honor for me to appear before the Committee on behalf of Philip Morris USA. HB 626 is a significant piece of legislation that impacts all tobacco categories and a number of important programs. While I have concerns about the impact on all of the tobacco categories, I would like to confine my comments to the proposed \$1.50 increase per pack in Montana's cigarette excise tax.

I would like to begin my remarks by reminding the Committee that effective April 1 of 2009, the federal excise tax on cigarettes increased by approximately \$0.61 per pack. Currently, the total excise tax, state and federal, on a pack of cigarettes in Montana is \$2.71. I ask Committee Members to keep this in mind as I discuss the following arguments against the \$1.50 proposed state excise tax increase.

Increasing taxes on tobacco products can be an unpredictable proposition. Over the years, states across the country, including Montana, have resorted to a tax increase on tobacco only to see revenues fall well short of their projections. In one case, such a tax actually caused tax revenues to decline. In October 2009, D.C.'s cigarette excise tax increased from \$2.00 to \$2.50 per pack.¹ The 50 cent tax increase was expected to raise an additional \$10 million in revenue in FY2010.² Not only has the cigarette tax increase failed to generate the projected additional local revenue, but there was actually a \$3.7 million decline in revenue in the twelve months following the tax increase..³

Total state tax-paid cigarette sales in the United States have declined by an average of 3.7% per year from 2001-2010.⁴ In FY2010, tax-paid sales declined by 8.3%.⁵ In Montana, tax-paid

¹ Government of the District of Columbia. Office of the Chief Financial Officer. February 24, 2010.

² DC Fiscal Policy Institute. "What's in the Amended FY 2010 DC Budget?" October 2, 2009.

³ Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

⁴ Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.



cigarette sales have declined by 4.1% a year for the last ten years.⁶ As a result, Montana will realize less revenue from a cigarette tax over time and will need to find other means to fill the future gaps in funding.

An issue of particular importance when considering a further tax burden on tobacco products is the effect it will have on the illicit tobacco trade. A tax increase could contribute to increased incentives for smuggling and other contraband activities. This may include buying tobacco products in other states and jurisdictions, on Native American reservations, over the Internet or at other similar venues, where taxes may not be collected at all. As stated by John D'Angelo of the Bureau of Alcohol, Tobacco, Firearms and Explosives, "There is no doubt that there's a direct relationship between the increase in a state's tax and an increase in illegal trafficking."⁷

The proposed cigarette excise tax will cause packs of cigarettes to be much more expensive in Montana when compared to its neighbors. The current tax per pack in Montana is \$1.70. If a \$1.50 per pack increase in the state cigarette excise tax were implemented, the tax would jump to \$3.20 per pack. Such a tax would far exceed any of our neighboring states – more than seven times that of North Dakota, (\$0.44) five times Idaho (\$0.57) and Wyoming (\$0.60), and more than twice that of South Dakota (\$1.53).⁸ The resulting per pack tax difference between Montana and its neighbors will provide incentives for adult smokers to cross the border to buy cigarettes in states with lower excise taxes.

Not only does the tax burden hurt average consumers, but it also works against small businesses that rely heavily on tobacco sales to stay afloat. Montana retailers stand to lose from a cigarette excise tax increase. Cigarette sales are an important source of revenue for many of Montana's approximately 1,610 retailers.⁹ According to the National Association of Convenience Stores, cigarette sales account for 35.9% of all in-store sales at convenience stores nationwide.¹⁰

⁵ Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

⁶ Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

⁷ Maria Schultz, *Raised Tax on Smokes May Stoke Illicit Sales*, DETROIT NEWS, (July 21, 2002).

⁸ Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

⁹ Retail locations based on internal PMUSA data and rounded to nearest 10.

¹⁰ *State of the Industry: Convenience Store Totals, Trends & Averages*, NATIONAL ASSOCIATION OF CONVENIENCE STORES, 2009.



Cigarette excise taxes currently provide a significant source of revenue for Montana. In fiscal year 2010, the sale of cigarettes in Montana generated \$78.5 million in state excise taxes.¹¹ This is in addition to the payments Montana received under the tobacco settlement agreement. Actual 2010 settlement payments were \$31.5 million, and have averaged \$30.8 million over the last five years.¹² PM USA believes that adult smokers in Montana already pay a fair amount of taxes on the cigarettes they purchase. The adverse economic impact this proposal would have on adult Montana smokers is another reason the cigarette excise tax should not be raised.

The Montana adult who purchases one pack per day already pays \$1,245 per year to the federal and state government.¹³ This is on top of the other taxes that a typical household may pay, including: income taxes, social security taxes, excise taxes on other products (such as gasoline), and property taxes. Including the proposed \$1.50 cigarette excise tax increase, the total government costs imposed on cigarettes could increase to as high as \$1,792 per year for an adult purchasing one pack per day.¹⁴

Should the proposed \$1.50 cigarette excise tax increase be enacted, adult smokers would be paying \$4.91 in government revenue for a pack of cigarettes in Montana, which would then account for approximately 63% of the total cost for a pack of cigarettes.¹⁵ The large share of cigarette revenues the government already receives should be strongly considered before any further tax increase is implemented.

Moreover, cigarette excise taxes are unfair and regressive, impacting lower-income adult smokers more than high-income adult smokers. This is because the taxes are placed on the product and not based on income level. Increasing the cigarette excise tax will disproportionately burden lower income households.

¹¹ Orzechowski, Bill & Walker, Rob, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

¹² Campaign for Tobacco Free Kids, "ACTUAL TOBACCO SETTLEMENT PAYMENTS RECEIVED BY THE STATES, 2002-2010"

¹³ This includes the state excise tax and federal excise tax paid by a pack a day smoker per year based on information from Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

¹⁴ This includes the state excise tax and federal excise tax paid by a pack a day smoker per year based on information from Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.

¹⁵ Total government revenue estimated amount includes: federal excise tax, state excise tax, proposed state excise tax increase, and estimated settlement expense, quota buyout and FDA user fee. The manufacturer's price is the list price of a pack of Marlboro® cigarettes to wholesale less off-invoice allowance and applicable terms as of December 6, 2010, excluding settlement agreement and federal excise tax payments. The existing excise taxes can be found in, Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc. The estimated settlement cost per pack and the estimated quota buyout payment are from PM USA internal data. The FDA user fee revenues are estimated based on total FDA user fee revenues and total national and state tax-paid sales. The estimated trade markup used in the calculation of sales tax is based on data from: State of the Industry: Convenience Store Totals, Trends & Averages, NATIONAL ASSOCIATION OF CONVENIENCE STORES, 2009.



Raising taxes on cigarettes by \$1.50 per pack would put in place a regressive tax at a time when citizens of Montana can ill afford it. The historic financial and economic crisis has led to exceptionally high levels of unemployment and eliminated significant wealth from the American economy. While it has also weakened state budgets across the nation, now is not the time to further strain households struggling to recover from this crisis with new tax increases.

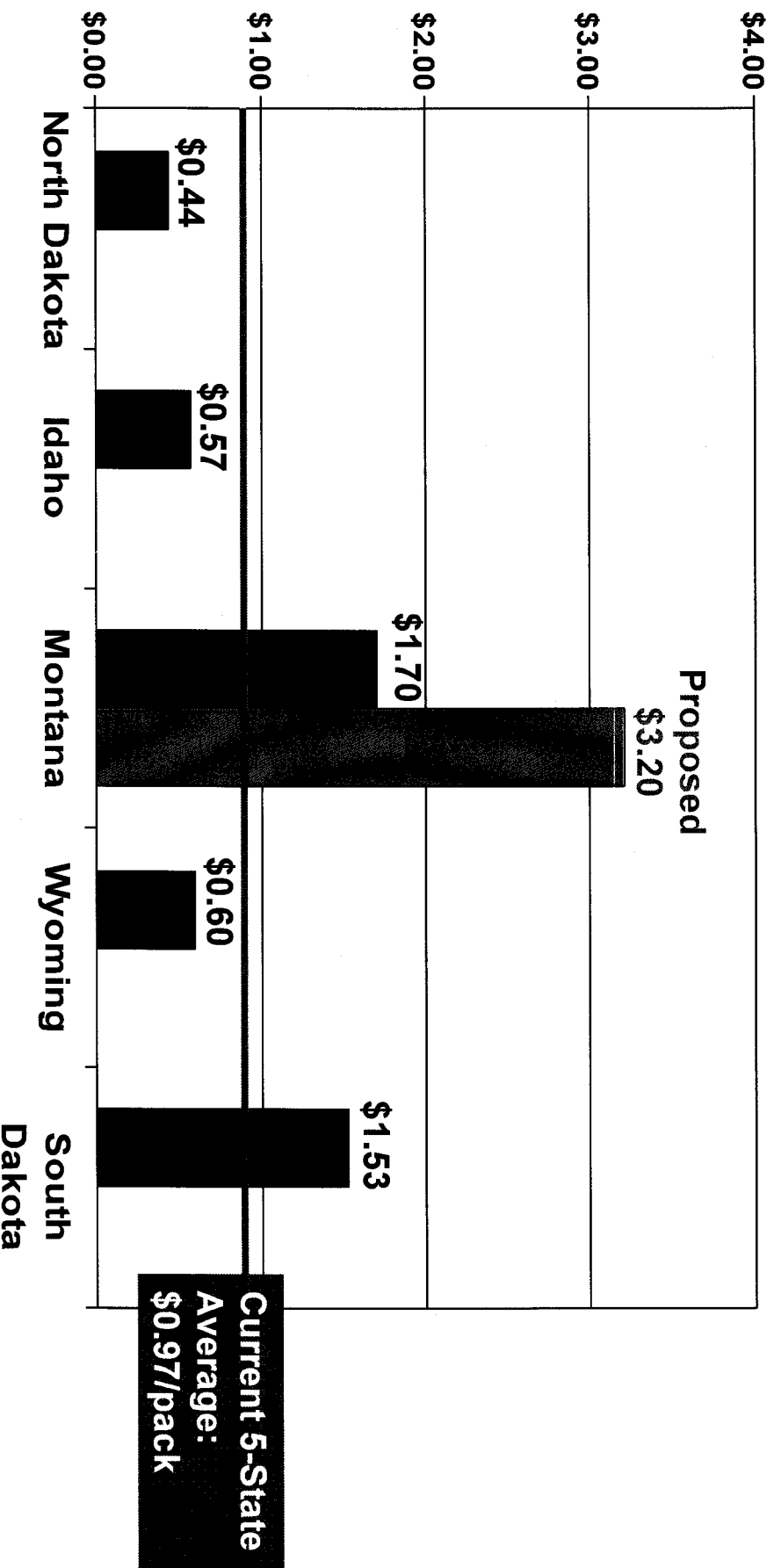
In addition to being regressive and unfair to adults who smoke, this increase will likely harm many legitimate businesses that operate here in Montana. For all of these reasons, please vote against HB 626 and reject this proposed tax increase.

Thank you for your time.



Information provided by Altria Client Services Inc. on behalf of Philip Morris USA Inc.
For more information please visit www.pmuusa.com

Regional Cigarette Excise Tax Rates



Source: Bill Orzechowski & Rob Walker, *The Tax Burden on Tobacco*, vol. 45 (February 2011); funded in part by Altria Client Services Inc.



Altria

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